ANNUAL REPORT

1997

Tier One Energy Corp.

CORPORATE PROFILE

Tier One Energy Corp. is an oil and gas exploration, development and production enterprise operating primarily in Alberta. This independent Canadian company has been public since December 31, 1996. Tier One's goal is to maximize shareholder value by the successful exploration and exploitation of internally generated opportunities. As a true full-cycle exploration and production organization, the Company has set its course to achieve ongoing growth and value primarily through the drill bit. This approach will, on occasion, be further strengthened by strategic asset purchases designed to consolidate our position within Tier One focus areas.

Tier One's success and continuing growth are based upon a strong financial framework. One forged by a management team whose unique combination of technical expertise, field experience and proven track record ensures a strong future for the Company.

The Company's Class A and Class B shares trade on the Alberta Stock Exchange under the trading symbols "TO.A" and "TO.B" respectively.

Table of Contents

Annual General Meeting

We encourage shareholders to attend the Annual General Meeting to be held Thursday, June 11, 1998 at 3:00pm in the Banff Room, The Westin Calgary, 320 – 4th Avenue SW, Calgary, Alberta.

Abbreviations

Boe	Barrels of oil equivalent
Boe/d	Barrels of oil equivalent per day
Bbls	Barrels of oil
Bbls/d	Barrels of oil per day
MBoe	Thousand barrels of oil equivalent
Mstb	Thousand stock tank barrels
MMCF	Million cubic feet of natural gas
Ooip	Original oil in place

Results & Objectives

1997 Results

- Drilled 29 gross wells (11.9 net) achieving a 90 percent success rate.
- Oil production averaged 133 Bbls/d and exited 1997 at 315 Bbls/d; exceeding our target rate of 300 Bbls/d.
- Increased proven and probable reserves to 1.4 million Boe.
- 1997 finding and development costs for proven and half probable reserves were $5.57/Boe.
- Capital expenditures for 1997 were $5.8 million. Of this total, $1.2 million was invested in the company's future through the acquisition of 15,000 acres of Crown Land and the completion of extensive seismic survey programs covering over 200 kilometres.
- In its first full year of operation, Tier One Energy Corp. recorded cash flow of $366,929 and positive net income of $45,916 on revenues of $918,728.

1998 Objectives

- Expand Tier One's light oil focus areas and increase production to the 1998 target exit rate of 600 Boe/d.
- Accelerate Tier One's goal of a balanced product portfolio by adding a focus area offering natural gas opportunities.
- Triple the Company's undeveloped land base by implementing a counter cyclical strategy, taking advantage of low oil prices and depressed land values.
- Maintain finding and development costs within a range of $5-$6/Boe.

FINANCIAL HIGHLIGHTS

FINANCIAL

For the year ended December 31, 1997		
Oil Sales (before royalties)		$1,005,022
Royalties (net of Alberta royalty tax credit)		$ (86,294)
Cash Flow from Operations		$ 366,929
Per Class A Share*	0.10	
Per Share (basic)**	0.05	
Per Share (fully diluted)**	0.05	
Net Income		$ 45,916
Per Class A Share*	0.01	
Per Share (basic)**	0.01	
Per Share (fully diluted)**	0.01	
Capital Expenditures		$5,756,574
As at December 31, 1997		
Working Capital Surplus		$ 719,980
Long-term debt		$ 750,000
Shareholders' Equity		$4,773,714
Total Assets		$7,786,766
Shares Outstanding		
Class A		3,411,719
Class B***		444,400
Stock Options (incl. issued & committed)		366,000

OPERATIONS

For the year ended December 31, 1997		
Average Daily Oil Production (Bbls/d)	133	
Exit Production Rate (Bbls/d)	315	
Average Product Sales Price		$ 22.35
Wells Drilled		
Gross	29.0	
Net	11.9	
Success Rate (%)	90.0	
As at January 1, 1998		
Reserves – Proved (Boe)		816,200
Reserves – Proved and Probable (Boe)		1,410,300
Undeveloped Land (Net Acres)		15,000

* These calculations exclude the conversion of the Class B shares and include all options.

** These calculations assume the conversion of the Class B shares at the maximum of 10:1.

*** The Class B shares convert before February 1, 2002 at a ratio of $10 divided by the greater of $1 and the then current market price of the Class A shares.

TIER ONE CORE VALUES

The following principles guide Tier One activities. They are reflected in the growth achieved in 1997. They are prevalent in the initiatives laid out for the current year. They are integral to the Company's long-term plans. Each principle plays a role in ensuring Tier One continues to deliver shareholder value.

- Growth will come predominantly through the drill bit.
- Tier One Energy Corp. will be a low cost producer. This is the touchstone against which decisions and results are measured.
- With an oil foundation in place, Tier One will pursue gas opportunities, moving towards the goal of a balanced product portfolio.
- Tier One will develop internally generated prospects in areas of proven hydrocarbon, multi-zone potential; enabling us to control the rate of development, product quality and costs.
- Tier One will support future growth by acquiring and maintaining a sufficient inventory of undeveloped land.
- Tier One Energy Corp. will maximize production and pursue projects offering immediate cash flow.
- Tier One will optimize use of debt under self-imposed debt guidelines. The Company's strategy is to limit debt to one times the forward year's cash flow.
- Tier One will progress towards operating 100 per cent of production and establishing 100 per cent working interest in all prospects.
- Tier One will use advanced technology to capitalize on exploration and exploitation opportunities.
- While following aggressive cash-flow targets, Tier One will avoid growth at the expense of net income.

Tier One's growth will come predominantly through the drill bit.

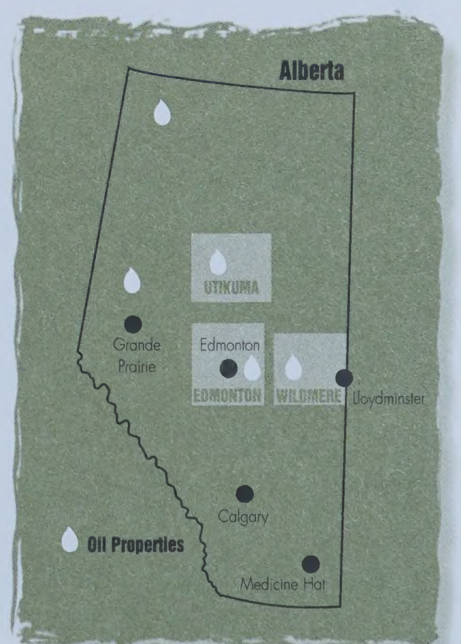
PRESIDENT'S MESSAGE

December 31, 1997, marked the completion of Tier One Energy Corp.'s first full year of operation. During this intense time our Company focussed on establishing a strong track record, proving our objectives could be realized in the field and in the marketplace. I am pleased to say the Company has met and exceeded its primary targets.

This year was characterized by an aggressive 29 well (11.9 net) drilling program that achieved a 90 percent success rate. Oil production volumes, which started the year at 26 Bbls/d, were targeted to exit at 300 Bbls/d, in fact reached 315 Bbls/d. Working through the highly competitive Crown Land Sales, Tier One had, by year-end, accumulated an undeveloped land base of 15,000 acres with an average 85 percent working interest.

The Company also established a high-quality drilling inventory within three focus areas: two newly established light oil areas, Edmonton and Utikuma, and our original focus area known as Wildmere. The latter clearly illustrates Tier One's philosophy, strategy and experience at work. The majority of the Company's 1997 growth resulted from drilling activity within Wildmere. Here, Tier One started with an exploitation opportunity and employed the latest technology to capitalize on a bypassed pay oil pool. With favourable results in place, Tier One shifted to optimizing production and full-scale development. The Company invested 81 percent of its 1997 capital expenditures in Wildmere, including the installation of a $2 million battery, waterflood facilities and pipeline system. This infrastructure will reduce 1998 operating costs to approximately $3.50/Bbl, making netbacks very attractive.

At Wildmere, Tier One has moved from bypassed pay opportunities to promising new finds. The Company has made this property a productive, cash flow generating site with ongoing development and exploration potential. This focus area is one example of how we plan to approach the further expansion of Tier One Energy Corp.



TIER ONE FOCUS AREAS

PRESIDENT'S MESSAGE

Disciplined Growth

In 1997, the Canadian oil and gas industry faced a very aggressive environment at every turn: inflated land sale prices; intense drilling programs; an overheated merger and acquisition market. During this time, Tier One reached its targets without following market pressures to "grow for the sake of growth." By adhering to the Company's core values, we avoided the Achilles' heel of many startup oil and gas companies – front-end dilution.

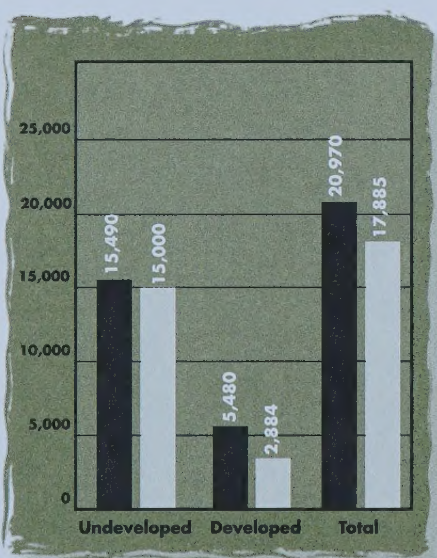
Two lines of thinking are at the root of Tier One's controlled expansion. First, growth comes primarily through the drill bit and is complemented by small strategic acquisitions. Such a purchase was made this past year when Tier One added a small asset base, previously owned by a major oil and gas producer. Located in the Utikuma area, this light oil property "fits" the Company's criteria and provides a promising entry point.

Second, Tier One targets prospects offering exploitation opportunities within a known region. This strategy, applied to all three focus areas, has already proven to be a cost-effective means of establishing a production base and gaining a foothold for further growth through exploration.

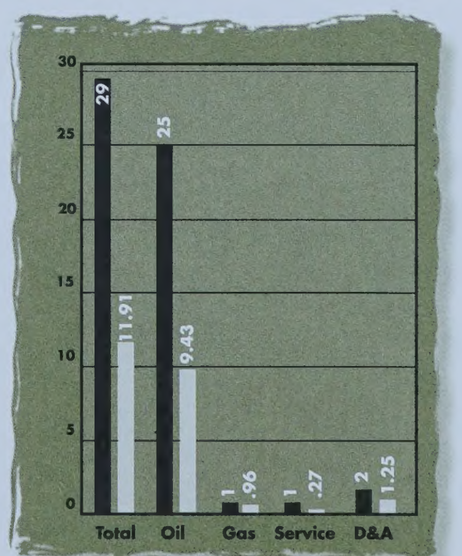
By choosing a prudent path to expansion, Tier One is well-positioned to take advantage of its current growth prospects and new opportunities arising in 1998.

Tier One's 1997 F&D costs were $5.57/Boe on a proven and half probable basis.

Tier One Energy Corp. drilled 76 percent of its wells.



LAND SUMMARY
Acres (to Dec. 31, 1997)



DRILLING RESULTS
Jan. 01 to Dec. 31, 1997

Gross
Net

LOOKING AHEAD

Over the last several months, Tier One has watched the crude oil "supply and demand" pendulum swing to the supply side, bringing the value of oil down swiftly. Several global factors are behind the drop in price from lofty 1997 levels. The ongoing effect of increased OPEC production, for instance, has been intensified by the precipitous fall of the Asian economic machine and the downward spiral of their respective currencies. In addition, these countries have cut refinery runs to levels matching domestic demand only, while unseasonable global weather patterns have reduced heating oil demands.

The Company recognizes these events to be part of a cyclical trend within the global oil market. The impact is already evident in the heavy oil arena where differentials have widened to all-time highs. This factor, combined with low prices, has caused the shut in of higher cost crude volumes. The impact of this situation on Tier One has been minimal.

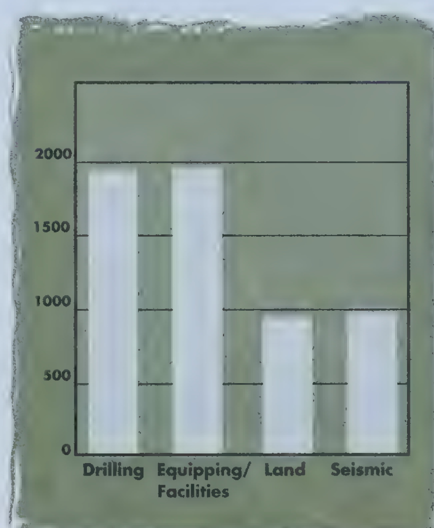
A Steady Course Amid Fluctuating Prices

To hedge the Company's position against these price fluctuations, Tier One constantly endeavours to maintain average operating costs at, or below, $5/Bbl. This allows us to maintain a healthy, flexible position in times of low prices. With the new Wildmere battery in place and development opportunities in hand, Tier One is well on its way to lowering operating costs throughout 1998.

Since all its major prospects are still demonstrating attractive economics at recent price levels, the Company will continue with planned capital expenditures. The current environment also gives us the opportunity to acquire healthy land positions at potentially lower prices.

Finding and Development Costs

In its first full year of operation, Tier One established F&D costs at the very respectable level of $5.57/Boe on a proven and half probable basis. This was achieved during a year where high commodity prices and the resulting infusion of capital produced rising F&D costs throughout the industry.



1997 CAPITAL EXPENDITURES
$ Thousands

As a full-cycle exploration and production company, $1.2 million (20 percent of 1997 capital expenditures) was dedicated to increasing Tier One's inventory of undeveloped land and seismic data. In keeping with traditional development time frames, the Company anticipates seeing initial benefits of this investment as early as 1998, with the full impact spread over the next two years.

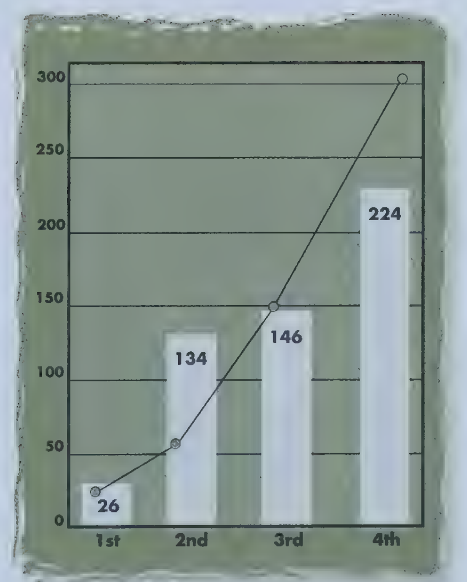
Room to Grow

The industry's ability, particularly that of junior oil companies, to raise equity during the early stages of 1998 has been curtailed. Tier One expects this situation to improve as commodity prices increase. The ability to manage debt levels within reasonable debt/cash flow ratios is critical at this time. I believe the market will, for the near-term, reflect positively on those companies that generate "success" from new discoveries and prudent exploitation, within a solid financial framework. Tier One Energy Corp. is strongly aligned with this position. As a result, the Company may initiate a share issue at a strategic point(s) during the year.

In terms of 1998 production, Tier One is focussed on doubling average volumes, with a target exit rate of 600 Boe/d. First, however, the Company expects to reach 500 Boe/d by the third quarter of 1998. This critical level will effectively push our general and administrative costs per barrel down and improve corporate profitability.

To achieve these objectives, the Company intends to maximize Wildmere production. Tier One will also dedicate significant resources to its Edmonton focus area and initiate exploitation and exploration work in Utikuma. In keeping with its long-term goal of balancing oil and gas production, Tier One will add a gas prone focus area to its inventory in 1998.

The Company will continue to employ a multi-faceted marketing strategy that has already achieved positive improvements to corporate netbacks. Tier One's aggressive approach demands we keep a constant eye on the marketplace, maximize opportunities and "work smarter" every step of the way.



1997 QUARTERLY OIL PRODUCTION

Barrels of oil per day (Bbls/d)
● Monthly Production

Human Resources

In January 1997, Tier One had two full-time team members: Earl Fawcett, Vice-President, Exploration and myself, Scott Dawson, President. Chris Willmann, a Consulting Geophysicist, has also been assisting us from the outset.

Over the past months, growing success, opportunities, and demands precipitated the addition of four new people. We have been pleased to welcome Richard Dahl, Vice-President, Engineering and Operations; Douglas Penner, Controller; Nadine Andreas, Geological Technologist; and Linda Lea, Land Analyst.

Tier One's achievements in 1997 are the direct result of an outstanding effort by this high-energy, highly skilled team. I would also like to officially welcome a new member to our Board of Directors. Mr. David Laws, President, Mutiny Oil and Gas Ltd., joined us on October 8, 1997.

This report provides a welcomed opportunity to thank staff for their dedication and the Board of Directors for their expertise and critical guidance.

To you, our shareholders I would add that Tier One Energy Corp. established a strong pace in its first full year. We accomplished our objectives, paving the way for your company to move forward with continued success in 1998 and beyond. Thank you for your ongoing support.

On behalf of the Board of Directors

A. Scott Dawson, P.Eng.
President and Chief Executive Officer

In Tier One's first full year of operation, revenues exceeded $900,000.

FOCUS AREAS

WILDMERE

Tier One's 11,000 net acres of undeveloped land, in the Wildmere focus area, offers an exceptional inventory of diverse opportunity. The potential product range, for the area situated along the identified GP trend, spans from low viscosity 21° API oil to 15° API heavy oil, all in significant long-life reserves. Wildmere gives Tier One a strong foundation for both short and long-term growth.

Tapping Immediate Cash Flow Opportunities

This past year, Tier One aggressively pursued the commercial opportunity our Wildmere General Petroleum "G" pool (GP "G") offers with its low viscosity (100 centipoise) 21° API oil. Our GP "G" pool slant drilling program resulted in 15 gross wells: for 11 oil wells, 2 injectors, 1 water source well and 1 D&A. The Company, which has a 27 percent working interest in this Wildmere property, increased volumes to a peak of 1,000 Bbls/d.

The Company constructed a $2 million battery, central waterflood facilities and pipeline system that will reduce operating costs throughout 1998 to an estimated $3.50/Bbl. In addition to our low cost structure, aggressive crude oil marketing strategies have already enabled us to realize $10/Bbl netbacks during low price periods.

Tier One also initiated a waterflood and anticipates receiving the Alberta Energy Utilities Board's (AEUB) GPP approval for the GP "G" Pool by June 1, 1998. We are forecasting average production of 600 Bbls/d for 1998. McDaniel & Associates Consultants Ltd. has identified 6.5 million Bbls of original oil in place (Ooip). To-date, the Company has only booked a 20 percent proven recovery factor. In this area, waterfloods typically increase recovery factors to a range of 30 to 35 percent of Ooip, which would, over time, add to our proven reserves.

1997 Wildmere Activities

Seismic Program:

- 9 km^2 3-D seismic survey completed
- 50 kms of 2-D seismic acquired

Drilling Program:

- 27 gross wells
- 9.3 net oil wells
- 0.96 net gas wells
- 0.27 source wells
- 1.25 dry and abandoned wells
- 87 percent drilling success rate

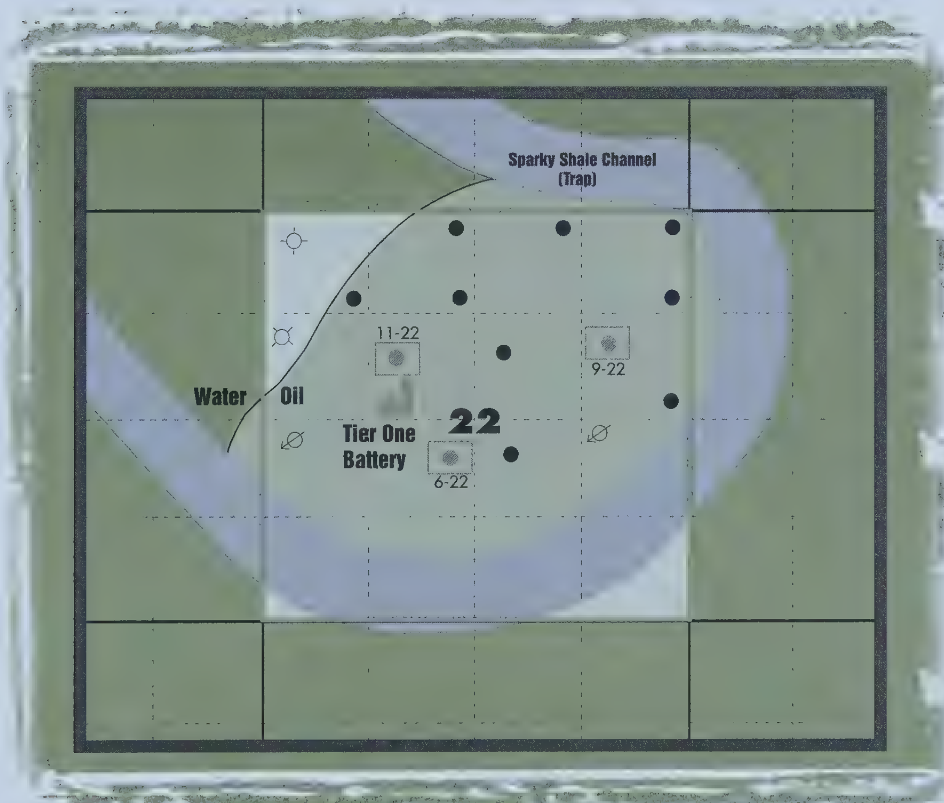
Future Opportunity

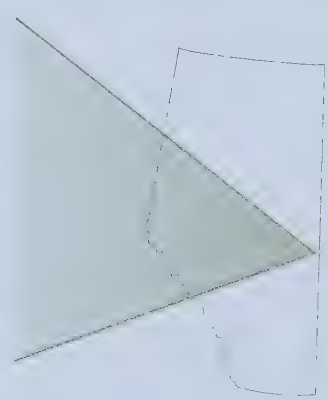
We have already identified five oil pools within the Wildmere focus area. Combined, these oil pools have significant unbooked reserves in place and are a valuable asset in our longer-term inventory. Tier One has an average 55 percent working interest in all five pools and plans to tap these quality reservoirs, beginning commercial development as heavy oil price differentials improve.

Focus on Wildmere

The Company plans to continue exploration along the medium-gravity Wildmere GP trend and has targeted three new pool wildcats for this year. Additional opportunities, within the heavy oil trend, include three already identified anomalies that will also be tested as differentials narrow.

Drilling featured five new pool wildcats, four oil and one gas – all of which are being evaluated for future development.



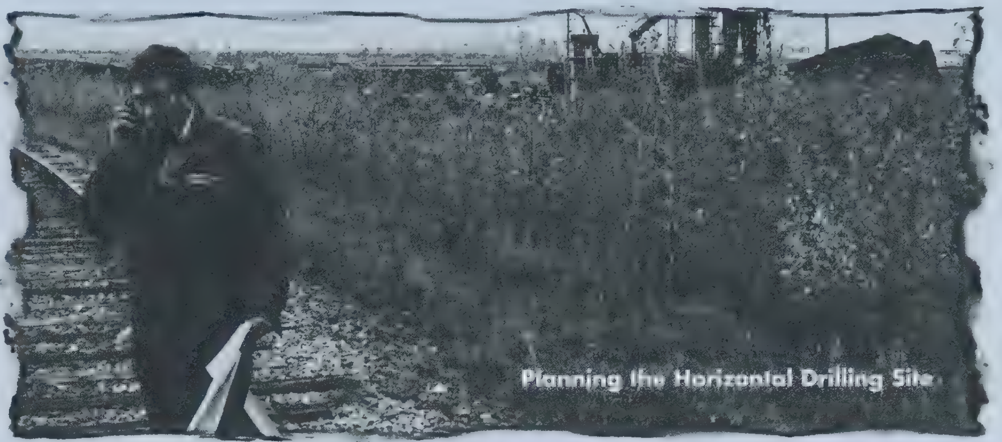


Tier One Lands

Slant Drilling Pad Sites

WILDMERE GP "G"POOL
WILDMERE FOCUS AREA

FOCUS AREAS



EDMONTON

Edmonton is a new focus area developed by Tier One in 1997. Through our ongoing land purchase program, we have accumulated an undeveloped base (to-date) of 2,600 acres at 100% interest. This proven hydrocarbon area offers several advantages: multi-zone potential; 27° to 35° API light oil; natural gas potential; quick access to market; and growth potential with extensive availability of Crown Land. We are particularly enthusiastic about two exploitation opportunities. First, we have secured the fee simple lands for the Chamberlain Basal Quartz Oil Pool, discovered in 1951 and abandoned in 1992. The AEUB recognizes 3.2 million Bbls Ooip with cumulative production to-date of 200,000 Bbls, equalling a six percent recovery factor.

Tier One plans to make the Edmonton area its number one focus for 1998.

We plan to exploit these reserves using horizontal drilling technology capable of increasing recovery factors to 30 to 40 percent. Our program will likely extend the current oil pool boundaries considerably. Given the depositional environment, we anticipate a marked increase in Ooip, reaching a potential 5–6 million Bbls. Drilling is scheduled to begin the second quarter of this year, with the opportunity for several follow-up locations to proceed throughout the balance of 1998. We expect initial productivity, based on start-up volumes of analogous horizontal wells, to reach 200 to 300 Bbls/d per well. Similar pools have reached total production rates of 1,000 to 2,000 Bbls/d.

Secondly, our Exploration department has identified a bypassed pay opportunity on our Morinville Prospect. A new well testing this zone, is slated for drilling in the second quarter of 1998.

Given the notable gas potential also identified in this region, the Company plans to make the Edmonton area its number one focus for 1998. Tier One has earmarked 40% of the 1998 capital budget for drilling and production on these prospects. Based on our initial results, this figure could increase significantly.

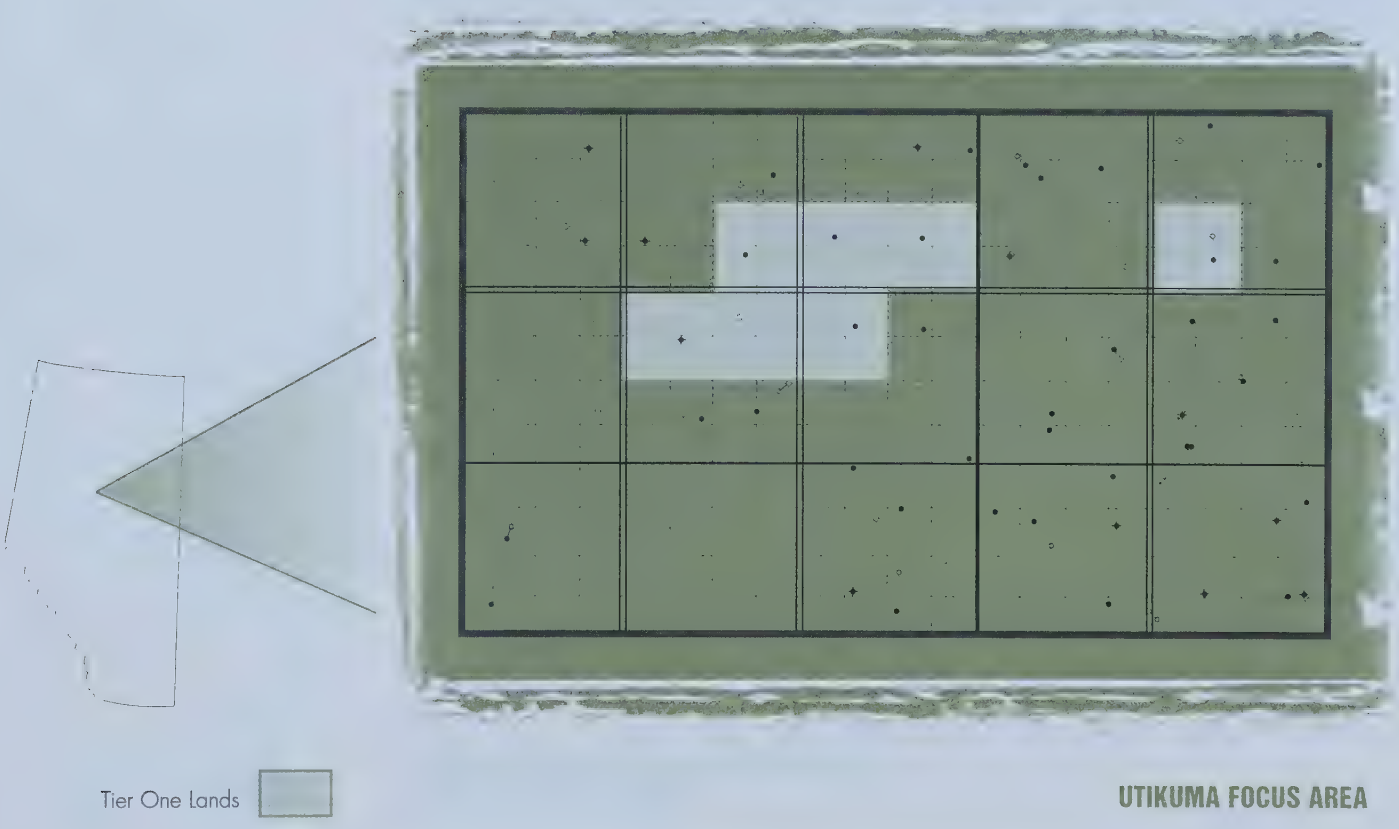
CHAMBERLAIN BASAL QUARTZ OIL POOL
EDMONTON FOCUS AREA

FOCUS AREAS

UTIKUMA

Located in north-central Alberta, Utikuma is Tier One's second new focus area. The Company completed this small property acquisition in the latter stages of 1997 and owns 100 percent working interest in 1,120 acres of land. This opportunity offers a sound entry point into a new region. The area is characterized by 40° API light oil with production stemming from several high-quality, medium-depth formations, primarily from the Gilwood and Keg River clastics.

Based on our interpretation of seismic data, we are confident two or three suspended well-bores on this property can be reactivated in 1998 using horizontal re-entry drilling technology. This will enable us to cost-effectively establish a production base, using existing pipeline and infrastructure, and will provide a starting point for further exploration. The Company projects 1998 Utikuma production volumes will reach 100 to 200 Bbls/d. A 3-D seismic program, being considered for late this year, will move forward as preliminary results are established.



UTIKUMA FOCUS AREA

CRUDE OIL & NATURAL GAS RESERVES

The volumes and present value of Tier One's petroleum reserves have been evaluated as at January 1, 1998 by McDaniel & Associates Consultants Ltd., independent petroleum engineers, in their report dated March 20, 1998 (the "McDaniel Report"). The "McDaniel Report" is summarized in the following tables. The present value of the estimated future revenue before tax to be derived by the Company's petroleum reserves includes ARTC.

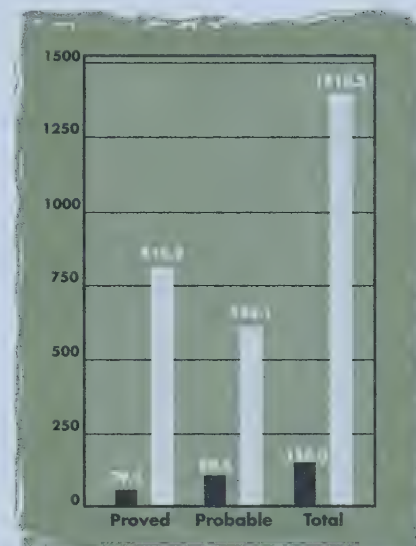
RESERVES

Reserve Volumes

As at January 1, 1998

Company's Share of Remaining Reserves (Before Royalties)

	Crude Oil Mstb	Natural Gas MMCF	MBoe (@10:1)
Proved Developed			
Producing	673.3	127.3	686.0
Non-Producing	–	601.6	60.2
Proved Undeveloped	70.0	–	70.0
Total Proved	743.3	728.9	816.2
Probable Additional	563.3	308.8	594.1
Total Before Risk	1306.5	1037.7	1410.3
Reduction due to Risk (½ Prob)	(281.7)	(154.4)	297.1
Total after Risk	1024.8	883.3	1113.1



1997 RESERVES RECONCILIATION CRUDE OIL & NATURAL GAS
(MBoe)
At January 1, 1997
At January 1, 1998

1997 Reserves Reconciliation

(Before Royalties)	Crude Oil		(Mstb)	Natural Gas (MMCF)			MBoe (@10:1)		
	Proved	Probable	Total	Proved	Probable	Total	Proved	Probable	Total
At Jan. 1, 1997	39.2	80.8	120.0	–	–	–	39.2	80.8	120.0
Discoveries	623.7	424.4	1048.1	708.1	298.6	1006.7	694.5	454.2	1148.7
Acquisitions	58.9	23.1	82.0	20.8	10.2	31.0	61.0	24.1	85.1
Production	(48.5)	–	(48.5)	–	–	–	(48.5)	–	(48.5)
Dispositions	–	–	–	–	–	–	–	–	–
Revisions	70.0	35.0	105.0	–	–	–	70.0	35.0	105.0
At Jan. 1, 1998	743.3	563.3	1306.6	728.9	308.8	1037.7	816.2	594.1	1410.3

Present Value of Estimated Future Net Revenue Before Tax ($ Thousands)

As at January 1, 1998

	Discounted at		
	10%	12%	15%
Proved Developed	6,748	6,401	5,943
Proved Undeveloped	164	113	56
Total Proved	6,912	6,514	5,999
Probable Additional	4,262	3,705	3,057
Total Proved plus Probable	11,174	10,219	9,056
Proved plus 50% Probable	9,043	8,366	7,528

Auditors' Report to the Shareholders

Tier One Energy Corp.
Year ended December 31, 1997 and for the period of incorporation on July 31, 1996 to December 31, 1996

We have audited the balance sheets of Tier One Energy Corp. as at December 31, 1997 and 1996 and the statements of earnings and retained earnings and changes in financial position for the year ended December 31, 1997 and for the period of incorporation on July 31, 1996 to December 31, 1996. These financial statements are the responsibility of the corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the corporation as at December 31, 1997 and 1996 and the results of its operations and the changes in its financial position for the year ended December 31, 1997 and for the period of incorporation on July 31, 1996 to December 31, 1996 in accordance with generally accepted accounting principles.

KPMG

KPMG
Chartered Accountants

Calgary, Canada
March 20, 1998

Balance Sheets

December 31, 1997 and 1996

	1997	1996
ASSETS		
Current assets:		
Cash	$ 570,063	$ 1,231,619
Accounts receivable	2,337,834	1,763,726
Inventory	28,075	–
Prepaid expenses	34,504	–
	2,970,476	2,995,345
Capital assets (note 3)	4,816,290	111,983
Incorporation costs	–	480
	$ 7,786,766	$ 3,107,808
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued liabilities	$ 2,250,496	122,643
Bank indebtedness (note 4)	750,000	–
Future site restoration	12,556	–
Shareholders' equity:		
Share capital (note 5)	4,727,085	2,984,452
Retained earnings	46,629	713
	4,773,714	2,985,165
Commitments (note 8)		
	$ 7,786,766	$ 3,107,808

See accompanying notes to financial statements.

Approved on behalf of the Board:

A. Scott Dawson
Director

Earl C. Fawcett
Director

F I N A N C I A L   S T A T E M E N T S

Statements of Earnings & Retained Earnings

Year ended December 31, 1997 and for the period of incorporation on July 31, 1996 to December 31, 1996

	1997	1996
Revenue:		
Production	$826,017	$52,814
Interest and other income	92,711	381
	918,728	53,195
Expenses:		
Operating	330,598	28,069
General and administrative	221,681	19,197
Depletion and depreciation	247,127	5,216
	799,406	52,482
Earnings before income taxes	119,322	713
Income taxes:		
Deferred	73,406	–
Net earnings	45,916	713
Retained earnings, beginning of period	713	–
Retained earnings, end of period	$ 46,629	$ 713
Earnings per common share	$ 0.01	$ –

See accompanying notes to financial statements.

Statements of Changes in Financial Position

Year ended December 31, 1997 and for the period of incorporation on July 31, 1996 to December 31, 1996

	1997	1996
Cash provided by (used in):		
Operations:		
Net income	$ 45,916	$ 713
Item not involving cash:		
Deferred income tax	73,406	–
Amortization of incorporation costs	480	–
Depletion and depreciation	247,127	5,216
Funds from operations	366,929	5,929
Changes in non-cash working capital	1,491,166	(1,641,083)
	1,858,095	(1,635,154)
Financing:		
Common shares, net of expenses	2,486,923	2,984,452
Bank indebtedness	750,000	(480)
	3,236,923	2,983,972
Investments:		
Additions to capital assets	(7,598,006)	(117,199)
Disposition of capital assets	1,841,432	–
	(5,756,574)	(117,199)
Change in cash	(661,556)	1,231,619
Cash, beginning of period	1,231,619	–
Cash, end of period	$ 570,063	$1,231,619
Funds from operations per share	$ 0.05	$ 0.01

See accompanying notes to financial statements.

Notes to Financial Statements

Year ended December 31, 1997 and for the period of incorporation on July 31, 1996 to December 31, 1996

1. Incorporation:

Tier One Energy Corp. (the "Corporation") was incorporated under the Business Corporations Act on July 31, 1996 as 704690 Alberta Ltd. On October 17, 1996, the Corporation changed its name to Tier One Energy Corp.

2. Significant accounting policies:

(a) Petroleum and natural gas properties:

The Corporation follows the full cost method of accounting for petroleum and natural gas operations whereby all costs related to the exploration for the development of oil and gas reserves are capitalized. These costs include land acquisition costs, geological and geophysical expenses, the costs of drilling both productive and non-productive wells and directly related overhead. Proceeds from the disposal of properties are deducted from the full cost pool without recognition of a gain or loss. When a significant portion of properties is sold, a gain or loss is recorded and reflected in the statement of earnings.

Depletion of petroleum and natural gas properties is provided. Natural gas reserves and production are converted to equivalent units of energy on a 6:1 basis.

The Corporation annually applies a ceiling test to capitalized costs to ensure that such costs do not exceed the costs of unproven properties plus future net revenues from production of proved reserves at year end product prices less future administrative, financing, site restoration, and income tax expenses.

Substantially all of the Corporation's exploration and development activities are conducted jointly with others and, accordingly, the financial statements reflect only the Corporation's proportionate interest in such activities.

Depreciation on office furniture and equipment is provided for on a 20% and 30% declining balance basis respectively.

(b) Future site restoration costs:

Future site restoration costs are based on management's estimates and amortized on the unit-of-production method over the remaining proved reserves. The provision is included in depletion and depreciation in the statement of earnings.

(c) Per share amounts:

Per share amounts are calculated using the weighted average number of Class A and Class B shares outstanding during the year.

(d) Flow-through shares:

Resource expenditure deductions funded by flow-through share arrangements are renounced to investors in accordance with income tax legislation. Petroleum and natural gas properties and share capital are reduced by the estimated cost of the renounced tax deductions when the expenditures are renounced.

(e) Inventory:

Inventory includes field and facility equipment which is carried at the lower of cost and net realizable value.

Year ended December 31, 1997 and for the period of incorporation
on July 31, 1996 to December 31, 1996

3. Capital assets:

1997	Cost	Accumulated Depletion & Depreciation	Net Book Value
Petroleum & natural gas properties	$4,997,142	$231,375	$4,765,767
Office furniture and equipment	58,935	8,412	50,523
	$5,056,077	$239,787	$4,816,290
1996			
Petroleum & natural gas properties	$115,130	$5,137	$109,993
Office furniture and equipment	2,069	79	1,990
	$117,199	$5,216	$111,983

Costs relating to acquiring and evaluating unproved properties totalling $1,196,000 (1996 – $nil) were excluded from the depletion and depreciation calculation.

At December 31, 1997, the estimated future site restoration costs to be accrued over the remaining proved reserves are $320,000 (1996 – $20,000).

4. Bank indebtedness:

The Company has available a $2,500,000 credit facility for general corporate and capital expenditures purposes with a chartered bank bearing interest at the bank's prime rate plus 0.5%. The credit facility is repayable on demand and is secured by a general assignment of book debts, a $10,000,000 fixed and floating charge debenture on certain properties and a floating charge over all other assets of the Company. The facility is renewable annually, however, no principal payments are required provided certain conditions continue to be satisfied.

5. Share capital:

(a) Authorized:

Unlimited number of voting Class A shares.

Unlimited number of voting Class B shares, convertible (at the option of the Corporation) at any time after December 31, 1999 and before December 31, 2001, into Class A shares. The fraction is calculated by dividing $10 by the greater of $1 and the then current market price of Class A shares. If conversion has not occurred by the close of business on December 31, 2001, the Class B shares become convertible (at the option of the shareholder) into Class A shares on the same basis. Effective on February 1, 2002, all remaining Class B shares will be deemed to be converted to Class A shares.

Year ended December 31, 1997 and for the period of incorporation on July 31, 1996 to December 31, 1996

(b) Issued and outstanding:

	Number of Shares	Amount
Class A shares		
Issued pursuant to public offering	1,515,000	$ 606,000
Issued to founders	750,000	150,000
Issued to acquire initial assets	750,000	35,815
Share issue costs	-	(505,363)
Balance, December 31, 1996	3,015,000	286,452
Issued on a flow-through basis	258,619	543,100
Issued on exercise of share purchase warrants	138,100	207,150
Share issue costs	–	(9,327)
Tax effect on share issue costs	-	73,406
Balance, December 31, 1997	3,411,719	1,100,781
Class B shares		
Issued pursuant to public offering (instalment option)	269,800	2,698,000
Balance, December 31, 1996	269,800	2,698,000
Issued pursuant to public offering (instalment option)	174,600	1,746,000
Tax benefit renounced relating to flow-through shares	–	(817,696)
Balance, December 31, 1997	444,400	3,626,304
Total		$ 4,727,085

(c) Share options:

As at December 31, 1997, 312,500 Class A shares of the Corporation were reserved for directors, officers and employees under the Corporation's stock option plans were outstanding at prices ranging from $0.60 to $2.00 per share and expiring in 2001 and 2002.

The Corporation is committed to grant an additional 53,500 options following additional issuance of Class A shares.

(d) Warrants:

Pursuant to the public offering, the Corporation issued 252,500 Class A share purchase warrants. Each warrant entitled the holder to purchase one Class A share at a price of $1.50 until December 31, 1997. During 1997, 138,100 warrants were exercised into Class A shares. The remaining warrants expired on December 31, 1997.

6. Related party transactions:

At December 31, 1997, there is $335,438 in accounts receivable and $2,329 in accounts payable which are owing from and due to related parties. Related parties are companies owned by officers and directors of the Company. Balances owing from and due to related parties occurred at normal trade terms according to the Joint Venture operating agreement.

Year ended December 31, 1997 and for the period of incorporation on July 31, 1996 to December 31, 1996

7. Income taxes:

The provision for income tax differs from the result which would be obtained by applying the combined Canadian Federal and Provincial income tax rate to income before taxes. This difference results from the following:

	1997	1996
Effective tax rate	44.6%	44.6%
Computed expected income tax	$ 53,241	$ 318
Effect on income tax of:		
Non-deductible crown royalties, net	34,615	864
Resource allowance	(38,692)	(815)
Non-deductible depletion	23,372	533
Other	870	(900)
Income tax expense	$ 73,406	$ –

Capital assets with a net book value as at December 31, 1997 of $930,000 (1996 – $27,000) have a nominal value for income tax purposes as a result of flow-through share issues.

At December 31, 1997, the Corporation had approximately $3,800,000 of resource and other unused income tax pools available to offset future taxable income.

8. Commitments:

Pursuant to the initial public offering, the Corporation issued 444,400 Class B flow-through shares for gross proceeds of $4,444,000. In addition, the Corporation issued 258,619 Class A flow-through shares for proceeds of $543,100. The Corporation has renounced $1,777,600 and had qualifying expenditures of $2,745,636 as at December 31, 1997. The Corporation is committed to $2,241,464 of exploration expenses eligible for renouncement for the year ended December 31, 1998 under the terms of the flow-through share agreements.

Future minimum lease payments relating to operating lease commitments on the building are:

1998	$ 49,500
1999	24,700
	$ 74,200

9. Financial instruments:

Financial instruments of the Company consist of cash, accounts receivable, prepaid expenses and accounts payable and at December 31, 1997 there are no significant differences between the carrying value reported on the balance sheet and their estimated market values.

CORPORATE INFORMATION

OFFICERS AND DIRECTORS

A. Scott Dawson	President, Chief Executive Officer and Director
Earl C. Fawcett	Vice-President and Director
Harley L. Winger	Director
Donald G. Cowie	Director
I. David Laws	Director

TIER ONE STAFF AND CONSULTANTS

A. Scott Dawson	President and Chief Executive Officer
Earl C. Fawcett	Vice-President, Exploration
Richard H. Dahl	Vice-President, Engineering and Operations
Douglas N. Penner	Controller
J. Chris Willmann	Consulting Geophysicist
Nadine M. Andreas	Geological Technologist
Linda J. Lea	Land Analyst

Auditors
KPMG, Chartered Accountants

Legal Counsel
Burstall Ward

Banker
National Bank of Canada

Evaluation Engineers
McDaniel & Assoc. Consultants Ltd.

Registrar & Transfer Agent
Montreal Trust Company of Canada

Exchange Listing
The Alberta Stock Exchange
Stock Symbol: **TO.A, TO.B**

Executive Offices

Suite 1400, 736 – 6 Avenue SW
Calgary, Alberta T2P 3T7
Tel: 403.205.3700
Fax: 403.205.3709

TierOne Energy Corp.

Suite 1400, 736 - 6 Avenue, S.W., Calgary, Alberta T2P 3T7
Tel (403) 205-3700 Fax (403) 205-3709